



Report of the Vermont State Auditor

April 2, 2008

INTERNAL CONTROLS

Results of Review at the Agency
of Natural Resources

Thomas M. Salmon, CPA
Vermont State Auditor
Rpt. No. 08-3

Mission Statement

The mission of the Auditor's Office is to be a catalyst for good government by promoting reliable and accurate financial reporting as well as promoting economy, efficiency, and effectiveness in state government.

This report is a work of the Office of the State Auditor, State of Vermont, and is not subject to copyright protection in the United States. It may be reproduced and distributed in its entirety without further permission from the State of Vermont or the Office of the State Auditor. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately. Please contact the Office of the State Auditor if you have questions about reproducing this report.

**THOMAS M. SALMON, CPA
STATE AUDITOR**



**STATE OF VERMONT
OFFICE OF THE STATE AUDITOR**

April 2, 2008

The Honorable Gaye Symington
Speaker of the House of Representatives

The Honorable Peter D. Shumlin
President Pro Tempore of the Senate

The Honorable James Douglas
Governor

Mr. George Crombie
Secretary of the Agency of Natural Resources

Dear Colleagues,

As part of our audit of the Comprehensive Annual Financial Report (CAFR) for the fiscal year ending June 30, 2007, we reviewed internal controls over financial reporting, and compliance with laws and regulations at several State organizations, including the Agency of Natural Resources. Our work was performed for the limited purpose of planning and performing this audit and would not necessarily identify all deficiencies in internal control over financial reporting.

We found that the Agency had appropriately designed controls in a number of areas, such as payroll. However, we also found internal control deficiencies in which improvements could be made. In particular, in two cases, reconciliations were not being performed between data in ANR systems and VISION, the State's principal financial system. We consider the absence of such reconciliations to be a significant deficiency because it is a key control to ensure the completeness, accuracy, and validity of information recorded in the State's financial reporting system.

I would like to thank the management and staff of the Agency of Natural Resources for their cooperation and professionalism. If you would like to discuss any of the issues raised by this audit, I can be reached at the phone number or email listed below.

Sincerely,

Thomas M. Salmon CPA

Thomas M. Salmon, CPA
State Auditor

132 State Street • Montpelier, Vermont 05633-5101
Auditor: (802) 828-2281 • Toll-Free (in VT only): 1-877-290-1400 • Fax: (802) 828-2198
email: auditor@state.vt.us • website: www.auditor.vermont.gov

Report

Introduction	1
Highlights	3
Background	4
Entity-level Controls	5
Payroll, Accounts Payable, and Revenue Control Activities	7
Conclusions	11
Recommendations	11
Management’s Comments and Our Evaluation	12
Appendix I: Response from the Agency of Natural Resources	16

Abbreviations

ANR	Agency of Natural Resources
CAFR	Comprehensive Annual Financial Report
COSO	Committee of Sponsoring Organizations
SAS	Statement of Auditing Standards
VISION	Vermont Integrated Solution for Information and Organizational Needs

Introduction

The mission of the Agency of Natural Resources (ANR) is to protect, sustain, and enhance Vermont's natural resources for the benefit of this and future generations. It is comprised of four departments,¹

- *Central Office.* Responsible for the leadership and oversight of all agency programs, financial management, personnel management, information systems management, legal services, and enforcement of laws and regulations other than those related to the Fish and Wildlife.
- *Fish and Wildlife.* Responsible for the conservation and management of Vermont's fish and wildlife resources and the protection of the State's threatened and endangered species.
- *Forests, Parks and Recreation.* Responsible for the conservation and management of Vermont's forest resources, the operation and maintenance of the state park system, and the promotion and support of outdoor recreation for Vermonters and visitors to the State.
- *Environmental Conservation.* Responsible for the conservation and management of the State's natural resources and protection of the public health through various grant, regulatory, technical assistance, and public information and education programs.

ANR is significant to the State's financial statements. For example, ANR is responsible for the Fish and Wildlife fund, a non-major governmental fund in which the use of revenues from sources such as licenses and federal grants is restricted by statute to fish and wildlife purposes. In addition, in fiscal year 2007, ANR accounted for approximately \$2.4 million and \$3.6 million in revenue from ski leases and sales of services in State parks, respectively.

In consideration of ANR's financial significance and in accordance with our internal control audit obligations related to the State's fiscal year 2007

¹In May 2007, Secretary Crombie announced plans to reorganize ANR and established 18 task forces to plan this effort. According to ANR, the agency will be organized into a series of centers that will consist of cross-disciplinary teams of agency professionals who will look at the full range of environmental issues in a holistic manner. A final reorganization plan is expected to be issued in the June-August 2008 timeframe with implementation to begin thereafter.

Comprehensive Annual Financial Report (CAFR),² our objectives were to assess ANR's internal controls over financial reporting, and compliance with laws and regulations related to its (1) entity-level controls,³ (2) payroll, accounts payable, and revenue⁴ control activities.⁵

Auditing standards define three types of control findings.⁶ First, a control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. The auditor must evaluate identified control deficiencies to determine whether these deficiencies, individually or in combination, are significant deficiencies or material weaknesses. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote⁷ likelihood that a misstatement of the entity's financial statements that is more than inconsequential⁸ will not be prevented or detected. A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.

²*Generally Accepted Auditing Standards* AU Section 150.02 (American Institute of Certified Public Accountants, Inc.). These standards require that auditors obtain a sufficient understanding of the entity and its environment, including its internal control, to assess the risk of material misstatement of the financial statements whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures.

³Entity-level controls can have a pervasive effect on the overall system of control activities and pertain to the organization as a whole. It encompasses the organization's control environment, risk assessment, information and communication, and monitoring activities.

⁴We did not review revenue controls at the Department of Environmental Conservation. Such controls were addressed as part of another audit, *State of Vermont: Auditors' Report as Required by OMB Circular A-133 and Related Information, Year ended June 30, 2007* (KPMG, March 28, 2008).

⁵Control activities are the policies, procedures, techniques, and mechanisms that enforce management's directives.

⁶*Statement on Auditing Standards (SAS) 112, Communicating Internal Control Related Matters Identified in an Audit* (American Institute of Certified Public Accountants, Inc., May 2006).

⁷SAS 112 states that the likelihood of an event is "more than remote" when it is at least reasonably possible.

⁸The term "more than inconsequential" describes the magnitude of potential misstatement that could occur. A misstatement is inconsequential if a reasonable person would conclude, after considering the possibility of further undetected misstatements, that the misstatement, either individually or when aggregated with other misstatements, would clearly be immaterial to the financial statements.

Highlights: Report of the Vermont State Auditor

Internal Controls: Results of Review at the Agency of Natural Resources

(April 2008, Rpt. No. 08-3)

Why We Did This Audit

As part of our audit of the State's fiscal year 2007 CAFR, we evaluated ANR's internal controls over financial reporting, and compliance with laws and regulations. Specifically, we reviewed the design of ANR's entity-level controls and payroll, accounts payable, and revenue control activities, but did not perform tests of effectiveness.

What We Recommend

We made a variety of recommendations pertaining to entity-level controls and accounts payable and revenue control activities. In particular, we recommended that ANR develop a formal risk assessment measurement and monitoring program, establish a committee responsible for monitoring and assessing internal controls, develop a process to ensure that accounts payable are recorded in the appropriate fiscal year, perform certain revenue reconciliations, and take action to ensure appropriate segregation of duties for revenue activities.

Findings

In general, ANR provided evidence that it utilized key entity-level controls, such as an internal justification and approval process to recruit and hire new staff. However, we found two control deficiencies in that ANR had not implemented either a formal risk measurement and monitoring program or an internal control evaluation mechanism. Through the risk assessment process, management determines how much risk is to be prudently accepted and strives to maintain risk within these levels. Such a process is important because managers can use risk assessments to determine the relative potential for loss in programs and functions and to design the most cost-effective and productive internal controls. In addition, ANR does not have an ongoing mechanism to evaluate its internal controls. According to the State's internal control guide, management should establish procedures that monitor the effectiveness of control activities. Such monitoring provides management the opportunity to identify and correct any control activity deficiencies or problems and to minimize the impact of unfavorable events.

ANR's control activities with respect to payroll, accounts payable, and revenue presented a more varied picture. On the positive side, ANR was able to demonstrate that it had an adequate design of payroll control activities. For accounts payable activities, ANR had some, but not all expected control activities in place. In particular, our testing of 51 disbursements made after the end of the fiscal year indicated that 14 percent should have been, but were not, recorded as accounts payable in fiscal year 2007, which is a control deficiency.

ANR's control activities regarding revenue had two control deficiencies, one of which we consider to be significant. The significant deficiency related to the lack of reconciliations performed between the State's primary financial system and systems that capture license and sales of service revenues at the Departments of Fish and Wildlife and Forests, Parks and Recreation, respectively. Reconciliations are a key control to ensure the completeness, accuracy, and validity of information recorded in the financial reporting system. The second control deficiency related to segregation of duties, which is the division of key duties and responsibilities among different people to reduce the risk of error or fraud. In this case, the Departments of Fish and Wildlife and Forests, Parks and Recreation were not following the State's internal control guidance, which sets out examples of incompatible duties.

Background

Internal control can be broadly defined as a process, affected by an entity's governance structure, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- effectiveness and efficiency of operations,
- reliability of financial reporting, and
- compliance with applicable laws and regulations.⁹

Internal control is a major part of managing an organization. Such controls comprise the plans, methods, and procedures used to meet missions, goals, and objectives. In addition, internal controls serve as the first line of defense in safeguarding assets and preventing and detecting errors and fraud.

Scope and Methodology

As part of our audit of the State's fiscal year 2007 CAFR, we gained an understanding of internal controls at the Agency of Natural Resources. Our work was performed for the limited purpose of planning and performing this audit and would not necessarily identify all deficiencies in internal control over financial reporting. We considered the design of the Agency's controls and whether they were in place and operational. We did not test the effectiveness of the controls.

To assess ANR's entity-level controls, we used guidance developed by the U.S. Government Accountability Office¹⁰ to develop a set of questions that addressed the agency's control environment, risk assessment, information and communications, and monitoring activities. We assessed the responses to these questions that were provided by ANR's Central Office and the

⁹This definition generally comes from the Committee of Sponsoring Organizations of the Treadway Commission (COSO), but we substituted the term governance structure for board of directors used in the original definition to make it more applicable to State government.

¹⁰*Internal Control Management and Evaluation Tool* (U.S. Government Accountability Office, GAO-01-1008G, August 2001).

Departments of Fish and Wildlife, Forest, Parks and Recreation, and Environmental Conservation. In addition, we reviewed and assessed applicable documentation, such as ANR's budget, strategic plans, recruiting and employee performance evaluation forms, and its internal control self-assessment.

As part of reviewing the payroll, accounts payable, and revenue control activities, we performed walkthroughs of these functions with applicable staff. In the case of payroll we also reviewed examples of a time report and exception reports from the State's time recording system. For the accounts payable function, we obtained a listing from the State's primary financial system—the Vermont Integrated Solution for Information and Organizational Needs (VISION)—of all disbursements made between July 1, 2007 and September 24, 2007. We performed a cut-off test of a sample of these disbursements to determine whether accounts payable were being recorded in the correct fiscal year. With respect to revenue control activities, in addition to the walkthrough, we performed analytical procedures and period-end cut-off procedures for the Department of Fish and Wildlife angler and hunter licenses and Department of Forests, Parks and Recreation sales of services.

We performed this audit in accordance with generally accepted government auditing standards between August and October 2007 in Waterbury.

Entity-level Controls

In general, ANR provided evidence that it employed key entity-level controls although some improvements could be made. Specifically, ANR had two control deficiencies in that it had not implemented either a formal risk measurement and monitoring program or an internal control evaluation mechanism.

ANR's entity-level controls encompass its control environment, risk assessment, information and communication, and monitoring activities, as follows.¹¹

¹¹To guide our assessment of entity-level controls, we generally utilized the internal control frameworks and definitions promulgated by COSO and the U.S. Government Accountability Office. These concepts are also included in State guidance on internal controls, *Internal Control Standards: A Guide for Managers* (Department of Finance and Management).

-
- *Control environment.* The control environment sets the tone of an organization. It is the foundation for all other components of internal control. Among the factors that influence an evaluation of an organization's control environment are ethical values and integrity, management philosophy and operating style, commitment to competence, and structure.
 - *Risk assessment.* Risk assessment is the identification and analysis of relevant risks to the achievement of the objectives of an organization, which forms the basis of determining how these risks should be managed.
 - *Information and communication.* For an entity to run and control its operations, it must have relevant, reliable information, both financial and non-financial, related to internal and external events. Effective communication must occur in a broad sense, flowing down, across, and up the organization.
 - *Monitoring.* Internal control environments need to be monitored. Ongoing monitoring occurs in the course of operations, including regular management and supervisory activities.

ANR provided evidence that it had implemented important controls in these areas. For example, as part of its commitment to competence within its control environment, ANR implemented an internal request form to obtain internal approval to recruit, reclassify a vacant position, or hire staff, which requires a description of job duties and a justification for the position. In addition, justifications to hire require a description of the selection process used and an explanation as to why it is thought that a particular candidate will be successful in the position.

However, ANR also had two control deficiencies in its entity-level controls. First, ANR had not implemented a formal risk measurement and monitoring program. All entities, regardless of size, structure, nature, or industry, encounter risks at all levels within their organizations. Through the risk assessment process, management determines how much risk is to be prudently accepted and strives to maintain risk within these levels. Such a process is important because, according to the State's internal control guidance,¹² managers can use risk assessments to determine the relative

¹²*Internal Control Standards: A Guide for Managers* (Department of Finance and Management).

potential for loss in programs and functions and to design the most cost-effective and productive internal controls.

Second, ANR does not have a formal internal audit function. The State's internal control guide states that management should establish procedures that monitor the effectiveness of control activities and the use of control overrides. ANR participates in an annual statewide internal control self-assessment process sponsored by the Department of Finance and Management and the Director of Administrative Services stated that he independently reviews processes and financial data across the Agency. However, the Director added that while he has reviewed a wide range of internal control areas he has not documented the results of these reviews. Without documentation it is not possible for us to evaluate the rigor and completeness of the Director's reviews. Moreover, the Director is reviewing processes for which he has oversight and, therefore, would not be as independent as an individual or committee that does not directly supervise the processes being reviewed. Reviews by management and/or supervisors are important, but could be enhanced by including others more independent of the process as part of the review. Also, a formal monitoring process gives management the opportunity to identify and correct any control activity deficiencies or problems and to minimize the impact of unfavorable events.

ANR also did not employ two common mechanisms that can assist in preventing and detecting fraud, particularly from internal sources. Specifically, ANR did not conduct background checks on employees with a high level of fiscal responsibility nor did it have a formal fraud prevention program. However, because we found that the State as a whole lacked these mechanisms, we will be addressing these issues on a statewide rather than on an organization-by-organization basis.

Payroll, Accounts Payable, and Revenue Control Activities

ANR's implementation of effective payroll, accounts payable, and revenue control activities was mixed. There were no control deficiencies in the payroll area, one control deficiency related to accounts payable, and two control deficiencies in the revenue area, one of which was significant. In particular, ANR did not consistently reconcile its underlying revenue records and systems related to angler and hunter licenses and State park fees to VISION—the state's principal financial system—which is a significant deficiency.

Payroll Control Activities

ANR was able to demonstrate that it had an adequate design of payroll control activities. For example, ANR provided copies of reports from the State's time recording system that listed exceptions, such as employees that did not have entries and employees whose timesheets did not pass certain edits. According to the ANR Central Office Business Manager, she and her staff review these reports and investigate errors prior to submitting the payroll information to the Department of Human Resources.

Accounts Payable Control Activities

In the case of accounts payable control activities, ANR had some, but not all, expected controls in place. An example of a control that was in place was ANR's invoice approval process. This process requires that invoices be reviewed and signed by the applicable authorizer prior to payment. In contrast, sufficient controls were not in place to ensure that accounts payables were recorded in the correct fiscal year. As part of its year-end closing procedures, the Department of Finance and Management required departments to add a "PY" prefix to the invoice number recorded in the State's principal accounting system (VISION) for all vouchers and journals entered in fiscal year 2008 that pertained to goods and services received or performed in the prior fiscal year.¹³ The proper coding in VISION of prior year payables through the use of the "PY" designation allows the State's Division of Financial Operations to extract relevant data from the system to record accounts payable in the correct fiscal year in the State's financial statements. At ANR, the Central Office performs the assessment of invoices paid subsequent to year-end to determine whether they should be designated with a "PY" in VISION.

Our review of 51 invoices with an accounting date of July 1, 2007 or later found that seven (14 percent) did not have the required "PY" prefix recorded in VISION even though they were for goods and services received in fiscal year 2007. Accordingly, these invoices were not recorded as accounts payable at the end of fiscal year 2007, which is a control deficiency. According to the Central Office Business Manager, there is no formal review process for evaluating whether invoices should have a "PY" designation. Instead, the applicable data entry staff are provided annual instructions. However, because of the number of errors that were found, additional

¹³*FY 2007 Year End Closing Instructions* (Department of Finance and Management, May 1, 2007).

training or reviews of invoices paid shortly after the end of the fiscal year may be needed.

Revenue Control Activities

In fiscal year 2007, the Department of Fish and Wildlife and the Department of Forest, Parks and Recreation recorded about \$5.2 million and \$3.6 million in angler and hunter licenses and sales of services revenues, respectively. In the case of the Department of Fish and Wildlife, angler and hunter licenses can be purchased online or through an agent. For those purchased through an agent, the department receives a copy of the application, a report of licenses sold, and a check. Fish and Wildlife financial staff record the revenue received from each agent in an internal license master database. With respect to sales of service revenue, attendants at the State's 52 parks collect and record sales in the Department of Forests, Parks and Recreation's VPark system. Both departments have implemented controls over their revenue processes. However, reconciliations with the State's principal financial system were not being performed and adequate segregation of duties was not always maintained.

A reconciliation process, whether manual or automated, is a necessary and valuable part of a sound financial management system. Both the Department of Fish and Wildlife and the Department of Forests, Parks and Recreation reported that they reconciled receipts received to data in their internal revenue systems; the master licensing database and the VPark system, respectively. This is an important control activity that helps ensure that monies received are recorded correctly.

The departments record detailed revenue transactions in their internal systems and summary-level data in VISION. The Department of Finance and Management has directed that all State departments that maintain an accounting system outside of VISION reconcile the activity in their systems to VISION as of the end of the fiscal year.¹⁴ However, the Department of Fish and Wildlife did not reconcile its licensing database for angler and hunter licenses to VISION. Similarly, the Department of Forests, Parks and Recreation did not reconcile the State park fees that it recorded in its VPark system to VISION. Financial personnel from these departments stated that they had tried to perform such reconciliations in the past, but had abandoned these efforts largely because of difficulty in addressing the difference in timing of when transactions are recorded in their internal systems versus

¹⁴*FY 2007 Year End Closing Instructions* (Department of Finance and Management, May 1, 2007).

when the summary-level transactions are recorded in VISION. We believe that such obstacles can be overcome since timing differences are not an unusual complicating factor in reconciliation processes. Accordingly, since the preparation of a reconciliation of underlying data to the general ledger is a key control to ensure the completeness, accuracy and validity of information recorded in the financial reporting system, the lack of such reconciliations is a significant deficiency.

Segregation of duties is the division of key duties and responsibilities among different people to reduce the risk of error or fraud. No one individual should control or perform all key aspects of a transaction or event. According to the State's internal control guidance, examples of incompatible duties are (1) individuals who receive cash who also authorize and record bank deposits in the accounting records and (2) individuals who receive revenue or make deposits who also reconcile bank accounts. The Departments of Fish and Wildlife and Forests, Parks and Recreation were not following this guidance and had staff who performed all key aspects of certain transactions, as follows:

- *Department of Fish and Wildlife.* Regarding angler and hunter licenses sold by agents, a single employee (1) is provided the checks by the person who opens the mail, (2) prepares the checks for deposit, (3) reconciles the revenue database entry to the receipts, and (4) performs the year-end reconciliation of licenses sold. This same employee also serves as a backup for entering monthly licensing revenues earned from each agent into the licensing database and, therefore, has access to this system.
- *Department of Forests, Parks and Recreation.* Park Rangers or their designees accept cash, checks or other forms of payment, perform reconciliations of daily receipts to the VPark system, and make deposits. The department's business manager explained that segregation of duties is difficult to achieve at some individual parks because staff sizes may be too small. We agree that at times it may be impractical to maintain a strict segregation of duties in small organizations. However, there are after-the-fact detective controls that can be put in place to mitigate the risk associated with a lack of such separation. The Department of Finance and Management has issued guidance for these types of situations and provided examples of alternative controls, such as increased hands-on supervision and active review by management of financial data and

reports.¹⁵ The Department of Forests, Parks and Recreation could consider such alternatives in those cases in which appropriate segregation of duties cannot be maintained.

According to the Association of Certified Fraud Examiners, asset misappropriation is by far the most common form of occupational fraud, particularly as it relates to cash (which it defined as including currency, checks, and money orders).¹⁶ As such, controls over revenue transactions that involve cash are particularly important. The lack of adequate segregation of duties or an acceptable alternative pertaining to angler and hunter licenses and State park revenues is considered a control deficiency.

Conclusions

ANR has implemented a myriad of internal controls related to the entity-level controls and payroll, accounts payable, and revenue control activities. Such controls improve the likelihood that the Agency is positioned to achieve reliability in its financial operations. Nevertheless, there were a number of areas in which improvements can be made, particularly as it relates to establishing risk assessment processes, recording accounts payable in the appropriate fiscal year, and controls over revenue. These improvements are expected to further enhance ANR's controls and ensure the reliability of its financial reporting.

Recommendations

The Secretary of the Agency of Natural Resources should:

- Develop a formal risk assessment measurement and monitoring program, which includes risk assessments in major operational areas.
- Establish a committee, comprised of financial and program managers within the agency, that is responsible for monitoring and assessing

¹⁵*Internal Control News* (Department of Finance and Management, June 2006).

¹⁶*2006 ACFE Report to the Nation on Occupational Fraud & Abuse* (Association of Certified Fraud Examiners, 2006).

internal controls related to significant operational areas. This committee should also monitor and follow up on corrective action plans.

- Direct Central Office to provide training and implement reviews of invoices that are paid shortly after the end of the fiscal year to ensure that services provided or goods received in the prior fiscal year are recorded properly in VISION such that accounts payable are recorded in the appropriate year.
- Direct the Department of Fish and Wildlife to reconcile, on a monthly and annual basis, the data in the database that is used to capture angler and hunter license sales to the VISION account used to record such revenues.
- Direct the Department of Forests, Parks and Recreation to reconcile, on a monthly and annual basis, the VPark database to the VISION account used to record such revenues.
- Direct the Department of Fish and Wildlife to eliminate the segregation of duties violation related to the staff member that has control over the angler and hunter licenses revenue process.
- Direct the Department of Forests, Parks and Recreation to analyze its current controls over the sales of services revenue stream at its various park locations and, where practical, implement appropriate segregation of duties. In those cases in which appropriate segregation of duties is not practical, the department should implement additional detective controls to mitigate the risks associated with this lack of segregation.

Management's Comments and Our Evaluation

On March 26, 2008, the Deputy Secretary of the Agency of Natural Resources provided comments on a draft of this report (see appendix I for a reprint of these comments). In general, ANR's comments addressed the actions that it planned to take in response to our findings. However, the agency did not fully agree with some of the findings pertaining to the Department of Fish and Wildlife. The following summarizes ANR's comments and our evaluation.

- *Risk Management.* ANR stated that it actively considers and manages organizational risk, but acknowledged that it does not conduct risk management and monitoring in one comprehensive program. In the short term, the agency stated that, by June 30, 2008, it planned to have (1) an

initial program draft completed and (2) documentation of its risk management activities. ANR added that it believes that a statewide template to meet the requirements of a risk management and monitoring program would be the most efficient approach to this issue. We agree and have made a recommendation to address this issue at a statewide level.¹⁷

- *Internal Control Evaluations.* ANR concurred with our recommendation in this area. The agency reported that it planned to use the Coordinating Oversight Board that it is in the process of putting in place as part of its reorganization to monitor and assess internal controls. In addition, ANR plans to document the level of internal audit activity and corrective action verification currently in place. The agency stated that it expected to have the Oversight Board and the documentation of existing activities in place by the end of fiscal year 2008.
- *Accounts Payable Year-end Controls.* ANR reported that it has drafted a procedure to address the problems found in this control activity. In addition, ANR stated that it planned to (1) distribute and review this new procedure with each department before the end of the fiscal year, (2) monitor compliance, and (3) conduct a management review of a random sample of 50 invoices in the July to September 2008 timeframe.
- *Reconciliations Between Subsidiary Systems and VISION.* In the case of the Department of Fish and Wildlife angler and hunting revenue, ANR agreed that no formal process has been established to reconcile cash received with what was recorded in VISION. However, the agency pointed out that the Department of Fish and Wildlife's licensing database was not intended to be a financial system. Nevertheless, ANR reported that the department is working with a contractor on a new licensing system that is expected to include reports that will enhance the department's ability to reconcile license sales to revenue reported in VISION. This system is expected to be operable by the end of 2008. In the meantime, the department plans to implement an interim reconciliation process for license revenues. Regarding the Department of Forests, Parks, and Recreation, ANR reported that the department had taken preliminary steps to analyze the possibility of creating a monthly and annual reconciliation process between VParks and VISION. This

¹⁷*Fiscal Year 2007: Report on Internal Controls Over Financial Reporting and on Compliance with Laws and Regulations* (SAO Report No. 08-6, March 31, 2008).

initial analysis highlighted the difficulty of performing such reconciliations. Nonetheless, the department plans to continue this analysis and to solicit assistance from ANR and the Department of Finance and Management. We continue to believe that it is important that the Departments of Fish and Wildlife and Forests, Parks and Recreation perform reconciliations between the systems that contain the detailed transactions and that also support the summary-level revenue that is recorded in VISION. Without such reconciliations, it is more likely that errors in the recordation of revenue in VISION would not be caught or would not be caught in a timely manner.

- *Segregation of Duties.* The Department of Fish and Wildlife did not agree that it did not have adequate segregation of duties related to revenue from angler and hunter licenses sold by agents. The department believes that its current process is sufficient and explained how it separated various duties among different staff. We agree that the Department of Fish and Wildlife has segregated many of the duties associated with angler and hunter license revenues. However, the department acknowledged that the same licensing staff member that prepares the cash receipts deposit listing also (1) reconciles cash receipts to license revenue recorded in the license database and (2) processes the year-end agent account reconciliation. In addition, this same staff member can access the records in the licensing database. Taken together, having all of these duties concentrated in the hands of a single individual makes cash receipts more vulnerable to errors or misappropriation. The Department also noted that the license database was not intended to be a financial system. In our opinion, the licensing database fulfills the role of a financial system because it is the system that contains the detailed support for angler and hunter revenue.

In the case of the segregation of duties finding related to the Department of Forests, Parks and Recreation, the ANR response reiterated the inherent staffing limitations faced by this department. Nevertheless, the department plans to consider enhancing its existing oversight processes and exploring implementing additional controls. Such an analysis would be consistent with our recommendation.

- - - - -

In accordance with 32 V.S.A. §163, we are also providing copies of this report to the Secretary of the Agency of Administration, Commissioner of the Department of Finance and Management, and the Department of Libraries. In

addition, the report will be made available at no charge on the State Auditor's web site, <http://auditor.vermont.gov/>.

Appendix I: Response from the Agency of Natural Resources



State of Vermont
Office of the Secretary
103 South Main Street, Center Building
Waterbury, VT 05671-0301

[phone] 802-241-3600
[fax] 802-244-1102

Agency of Natural Resources

March 26, 2008

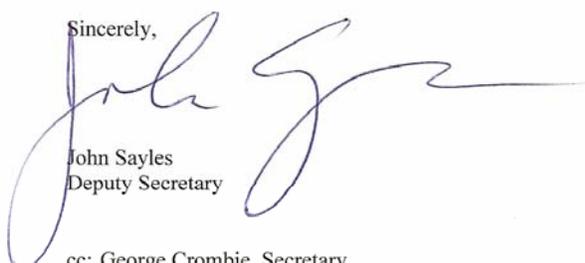
Thomas M. Salmon, CPA
Vermont State Auditor
132 State Street
Montpelier, Vermont 05633-5101

Re: Reply to Internal Control Audit of Agency of Natural Resources

Dear Mr. Salmon:

Attached is the Agency of Natural Resources response to the findings in your office's draft internal control review. The agency appreciates the opportunity to work with your office on improving internal controls, and looks forward to a continuing productive relationship.

Sincerely,


John Sayles
Deputy Secretary

cc: George Crombie, Secretary
Steve Chadwick, Administrative Services Director



Department of Fish & Wildlife . Department of Forests, Parks & Recreation . Department of Environmental Conservation

Appendix I: Response from the Agency of Natural Resources

**Agency of Natural Resources Response to the FY 2007 Internal Controls Review by the
Vermont State Auditor – March 17, 2008**

Formal Risk Measurement and Monitoring Program:

The Agency acknowledges that it does not conduct risk management and monitoring in one comprehensive program, but does recognize the value of a comprehensive program that includes assessment, prioritization methodologies, and action plans to mitigate and minimize risk. The Agency does actively consider and manage organizational risk in a wide range of areas including in financial management, emergency and disaster planning, data protection, workforce planning, continuity of operations, and information technology security.

The Agency believes that a statewide template including all key minimum elements is the most efficient approach for ensuring that all Departments and Agencies meet the requirements of a risk management and monitoring program, and it will pursue this with a plan to be an active part of an administration-wide work group in this effort.

In the short term the Agency has begun research including discussions with the Office of State Auditor staff, with other Agencies and Departments and through on-line searches for program guidelines and requirements. We plan to have our initial program draft completed by 06/30/08 along with documentation of our current risk management activities. Additional measurement and monitoring activities and action plans will be implemented shortly after that.

Internal Control Evaluation Mechanism:

We concur with the report recommendations to have a cross-functional committee responsible for monitoring and assessing internal controls relating to significant operational areas. In fact, through our Agency reorganization we are planning the establishment of the Center for Finance and Administration which will include a Coordinating Oversight Board that will be an excellent fit for meeting this purpose. We intend to have this in place before fiscal year '08 end.

We further plan to put into place the documentation to demonstrate the level of internal audit activity and corrective action verification currently in place and will formalize this program as well also by the end of the '08 fiscal year.

Accounts Payable Prior Year Invoice Recording:

In regards to the finding concerning Prior Year Payables being designated as such in the VISION accounting system, and thusly reflected accurately in the Comprehensive Annual Financial Report, the following actions will be taken:

A procedure has already been drafted which will address this finding by requiring invoice approvers in each department of ANR to clearly identify whether each invoice is for a prior year service or a current year service and to initial it as such. (Completed)

Appendix I: Response from the Agency of Natural Resources

This procedure will be distributed and reviewed with each department's financial group prior to the close of the fiscal year. (June 2008)

Compliance with the policy will be monitored and appropriate "PY" designation included in the VISION voucher entry and then initialed by the Central Office individual responsible for voucher entry on each invoice created during the first three months of the fiscal year. (July - September 2008)

A management review of a random sample of 50 invoices will be performed by the Assistant Director of Administrative Services and documented as to compliance at the end of each of the first three months of the fiscal year. (July -September 2008)

Revenue Control Activities – Reconciliation Process in Fish and Wildlife

The Department does not completely agree with this finding. It does agree that no formal process has been established to reconcile cash received for deposit with the deposits recorded in the VISION system. The Department is in the process of establishing a process that will reconcile revenues received for deposit with revenues recorded in the VISION system. This should be completed by 3/31/08. In addition, the Department will work with the vendor that is currently creating a new point of sale license system for the Department to ensure this system will be designed to provide sufficient reports to enhance the ability to reconcile license sales with revenues deposited into VISION. This new system should be available by the end of 2008 and will replace the current database. Once this new system is operable, the Department will reconcile license sales with VISION on a regular basis.

The primary purpose for the license database is to recording of the number and types of licenses sold for law enforcement purposes and to comply with Federal certification requirements of number of licenses sold. This certification determines the amount of Vermont's apportionment of Federal Wildlife and Sport Fish Restoration funds. Note that the Department is audited by the Federal government every few years (last audit FY06) and the accounting of our license sales for Federal programmatic purposes has always been found acceptable. The database was not intended to be a financial system. Because the Department is implementing a separate financial reconciliation process and a new license sales system, it does not believe it is prudent to develop a reconciliation process between the Department's existing license database and the VISION system.

Revenue Control Activities – Segregation of Duties in Fish and Wildlife:

The Department does not agree with this finding. We believe we have adequate segregation of duties. There is separation between receiving the cash, preparing the deposit slip and approving the deposit's entry into the VISION system, as outlined below.

The Department of Fish and Wildlife minimizes the number of employees who actually handle the cash before it is deposited, in accordance with the State's internal control guidelines. Once cash is received, checks are restrictively endorsed with a "for deposit only" stamp and put in a locked safe until a deposit is prepared. This cash may be received and put in the safe by either of

Appendix I: Response from the Agency of Natural Resources

the two license division staff. One licensing division staff member is responsible for preparing a receipt sheet that details cash received and ready for deposit. This receipt sheet is then hand delivered to ANR Admin Services. Admin Services staff are responsible for verifying the receipt sheet's amount, preparing the bank deposit slip, delivering the deposit to the bank, and entering the deposit information into the VISION system. After the deposit has been entered into the VISION system, a Fish and Wildlife business office staff member approves the deposit in VISION, referencing a copy of the receipt sheet that had been prepared by the licensing division.

It is the Department's opinion that, due to the fact that there are at a minimum two staff members beyond the licensing staff, one each from Admin Services and the Fish and Wildlife business office, involved in the deposit process there is sufficient segregation of duties with regards to cash receipts and deposits.

The auditor's finding was based on the fact that the same licensing staff that prepares the receipt sheet also reconciles revenues in the license database and processes year end agent account reconciliations. As stated above, the license database is not and was never intended to be used as a financial system. Staff are reconciling the number of licenses sold on the agent's report, to the number of licenses assigned to each agent to sell in a given calendar year.

The new licensing system currently being developed will eventually automate the vast majority of, or all, license sales. It is the Department's intention to have the system generate reports that will more clearly detail license sales, including the number and type of licenses sold and the amount owed to the State by each agent. This should allow for an easier process of reconciling both license sales and cash received. For now the Department has established a process that requires a supervisor's review and approval of all receipt sheets prior to their delivery to Admin Services.

Revenue Control Activities – Reconciliation Process in Forests, Parks and Recreation:

The Department of Forests, Parks & Recreation (FPR) acknowledges that currently no monthly or annual reconciliation process exists between the VPark system and VISION. However, it is important to note that VPark is used to reconcile weekly deposits from the Parks system into VISION.

Over the next 6 months, FPR will analyze the possibility of creating a monthly and annual reconciliation process between VPark and VISION. Preliminary steps have been taken in that FPR recently conducted a meeting to analyze and assess the Parks revenue collection process with the FPR business office, Parks management and the Agency's business office. This analysis highlighted the difficulties with reconciliation. Difficulties include timing of deposit differences and accounting for coupons or gift certificates.

Going forward, FPR plans to solicit assistance in developing a monthly and annual reconciliation process from both the Agency business office staff and the Department of Finance and Management's internal audit group.

Appendix I: Response from the Agency of Natural Resources

Revenue Control Activities – Segregation of Duties in Forests, Parks and Recreation:

As acknowledged by the State Auditor's office, in many State Parks, segregation of duties is impossible due to the small level of staffing. The Audit report referenced an Internal Control Newsletter published by the Department of Finance and Management in June 2006. FPR believes that it has, to some degree, implemented two of the recommendations (increased, hands-on supervision and active review by management of financial data and reports). The remaining recommendations are not possible in the operating structure of the State Parks' system given the inherent staffing limitations.

Regional supervisors have a strong presence and provide oversight to staff at Park locations. However, FPR will look at the possibility of enhancing this oversight. This may include more frequent site visits or remote review of financial reports. In addition, FPR will explore a more active review of financial data and reports from the Parks. This could include revenue trends by parks to determine irregularities. Over the next six months, FPR will study these two recommended control activities and explore additional potential controls given inherent staffing limitations.